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No. 04-751

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

H&R BLOCK, INC.; H&R BLOCK TAX SERVICES, INC.; H&R BLOCK EASTERN TAX SERVICES, INC.; ROBERT HECKERT; CYNTHIA LANTZ; CLARANCE MILLER CARLA R. LEWIS; DEBRA RIGGLEMAN; AND JOHN DOE,
Petitioners,

v.

DEADRA R. CUMMINS; IVAN BELL; AND LADONNA BELL, ON THEIR OWN BEHALF AND ON BEHALF OF THOSE SIMILARLY SITUATED,
Respondents.

On Petition for a Writ of Certiorari to the Circuit Court of Kanawha County, West Virginia

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REPLY BRIEF OF PETITIONERS

MATTHEW M. NEUMEIER
JENNER & BLOCK LLP
1 IBM Plaza
Chicago, IL 60611
(312) 222-9350

PAUL M. SMITH *
DUANE C. POZZA
JENNER & BLOCK LLP
601 13th Street, N.W.
Washington, D.C. 20005
(202) 639-6000

* Counsel of Record

Attorneys for Petitioners

WILSON-EPES PRINTING CO., INC. – (202) 789-0096 – WASHINGTON, D. C. 20001

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REPLY BRIEF OF PETITIONERS

Nearly all of respondents' arguments boil down to the claim that when an arbitration agreement includes a waiver of the right to bring a class action, a state court may, consistent with the Federal Arbitration Act (FAA), void the waiver of class actions as too "exculpatory" of small claims and then proceed to deny enforcement of the arbitration agreement itself. That is indeed the approach mandated in West Virginia by *State ex rel. Dunlap v. Berger*, 567 S.E.2d 265 (W. Va. 2002), and followed here. But contrary to respondents' repeated contentions, there remains a very substantial *federal* question whether the courts of West Virginia -- and the other courts around the country that refuse to enforce arbitration agreements if they also bar class adjudications -- are violating the FAA. Moreover, the federal issue is just as substantial when it comes to the additional ruling below that a court may completely disregard the parties' agreement to arbitrate challenges to the validity and enforceability of an arbitration agreement. Given the disarray in the lower courts on these matters and the importance of the issues, the Court should take this opportunity to address the questions presented by petitioners.

1. As respondents acknowledge, under the FAA, courts are required to put arbitration agreements on an equal footing with other contracts, denying enforcement only for reasons that would apply equally to any other type of agreement. Respondents argue that the court below obeyed that requirement because the principles of state law on which it relied -- the doctrine of unconscionability and the rule barring "exculpatory" clauses in contracts -- are also applied in West Virginia outside the context of arbitration agreements. But the mere fact that the court invoked state contract law in the course of deciding not to enforce an arbitration agreement does not immunize its ruling from

scrutiny under the FAA.[1] The question remains whether the effect of the court's ruling was to disfavor arbitration agreements in a way that Congress forbade.

The West Virginia rule barring parties' waiver of class action procedures effectively mandates that an arbitration agreement, to be enforceable, must allow arbitration of class claims. That may not be quite as extreme as treating all arbitration clauses in consumer contracts as unconscionable *per se* -- a rule that would clearly violate the FAA, *see Dunlap*, 567 S.E.2d at 277 (citing *Doctor's Associates, Inc. v. Casarotto*, 517 U.S. 681 (1996)). But it is at least highly doubtful that the FAA allows a court to condition its enforcement of an arbitration agreement on defendants' willingness to accept classwide arbitration -- because the *effects* of that rule approach a flat ban on arbitration clauses.

The whole point of the FAA is to encourage agreements to resolve disputes using a procedure that is more informal, speedy and efficient than court adjudication. The statute evinces an "unmistakably clear congressional purpose that the arbitration procedure, when selected by the parties to a contract, be speedy and not subject to delay and obstruction in the courts." *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 404 (1967); *see* H.R. Rep. No. 68-96, at 2 (1924) (FAA was meant as response to "agitation against the costliness and delays of litigation"). Requiring a potential defendant to accept class arbitration or forsake arbitration altogether effectively defeats the accomplishment of this congressional purpose.

While some courts have recognized and even encouraged class arbitration proceedings, they have also recognized that

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[1] *See* Stephen J. Ware, *Arbitration and Unconscionability After* Doctor's Associates, Inc. v. Casarotto, 31 Wake Forest L. Rev. 1001, 1015-16, 1034-35 (1996) (noting that equitable unconscionability holdings may still discriminate against arbitration and run afoul of the FAA).

such a process must be a "hybrid" in which the courts continue to play a very active role. *See generally* Jean R. Sternlight, *As Mandatory Binding Arbitration Meets the Class Action, Will the Class Action Survive?*, 42 Wm. & Mary L. Rev. 1, 37-42 (2000). As the California Supreme Court put it:

> Without doubt a judicially ordered classwide arbitration would entail a greater degree of judicial involvement than is normally associated with arbitration . . . . The court would have to make initial determinations regarding certification and notice to the class, and if classwide arbitration proceeds it may be called upon to exercise a measure of external supervision in order to safeguard the rights of absent class members to adequate representation and in the event of dismissal or settlement.

Keating v. Superior Court, 645 P.2d 1192, 1209 (Cal. 1982), *rev'd on other grounds*, 465 U.S. 1 (1984). Other courts have also recognized the need to become involved in such additional matters as the selection of the arbitrator and the management of discovery. *See* Sternlight, *supra*, at 40-42.

Clearly, this kind of complex process, in which the court may continue to play virtually every role other than the finder of fact, was not what Congress had in mind when it passed the FAA. And a potential defendant, when told by a state like West Virginia that this is the only form of arbitration that can be mandated in an enforceable consumer contract, would very likely question the point of asking for an arbitration agreement at all. Given how little class arbitration resembles the simple, quick and informal process the FAA was intended to encourage, there is little *practical* difference between (1) a rule barring all arbitration agreements as

unconscionable (which is clearly unlawful) and (2) a rule barring waivers of class actions in arbitration agreements. It follows that there is a very serious federal question presented concerning whether the latter rule comports with the FAA -- a question that cannot be swept under the rug on the theory that the court below was merely applying state contract law.[2]

Indeed, respondents' argument that state contract law was applied here in full compliance with the FAA becomes all the more unpersuasive when one recognizes that, in West Virginia, a defendant who even tries to insist on dealing only with consumers who agree to arbitrate disputes individually forfeits all rights to arbitrate. In both *Dunlap* and this case, the courts refused to sever the waiver of class actions from the rest of the arbitration agreements and *thus refused to give the defendant even the option of class arbitration*. *See* Pet. App. 14a; *Dunlap*, 567 S.E.2d at 283-84. This additional wrinkle in the courts' analysis further dramatizes the courts' antipathy to arbitration agreements and belies the notion that they are simply applying general state law rules barring exculpatory clauses in consumer contracts in a neutral

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[2] Another problem with the argument is that its very premise is wrong as a matter of West Virginia law. The prior cases invalidating "exculpatory" clauses outside the arbitration context cited in *Dunlap* and cited again here by respondents do not bear the remotest resemblance to the arbitration agreement at issue. They involved form contracts expressly waiving potential liabilities. *See Murphy v. North American River Runners, Inc.*, 412 S.E.2d 504, 510 (W. Va. 1991); *Hill v. Joseph T. Ryerson & Son, Inc.*, 268 S.E.2d 296, 307 (W. Va. 1980); *Dunlap*, 567 S.E.2d at 275 (citing *Murphy* and *Hill*); Opp. 11-12. An agreement requiring that claims be adjudicated individually rather than on a class basis is hardly exculpatory in that sense. And there is no case in West Virginia holding a waiver of the right to bring a class action unconscionable not involving an arbitration agreement. So the reality is that the West Virginia courts have stretched to reach this result only in the arbitration context.

manner.[3] The fact of the matter is that the West Virginia courts have searched for a way to evade their obligations under the FAA and the insistence on maintaining the right to bring a class action provided a convenient mechanism.

Moreover, they are not alone. As noted in the Petition, while there is wide disagreement around the country on these issues, there are a number of other jurisdictions in which arbitration agreements are only enforceable if they allow class arbitration. Respondents dismiss the conflicting cases as reflecting divergent state laws, Opp. 13, but those rulings also diverge in their interpretation of the FAA as applied to an arbitration agreement waiving class actions. *Compare Leonard v. Terminix Int'l Co., L.P.*, 854 So. 2d 529, 538-39 (Ala. 2002) (addressing federal law and finding unconscionability of class action waiver consistent with FAA) *with AutoNation USA Corp. v. Leroy*, 105 S.W.3d 190, 199-200 (Tex. App. - Houston [14th Dist.] 2003, no writ) (addressing federal law and holding that class action waiver could not be found unconscionable under the FAA). No matter how much respondents wish that only state law was involved, the mandates of the FAA are unavoidable in this and other cases involving class action waivers. Clearly, there is a glaring need for clarification of *how* the FAA applies when courts use the existence of a class action waiver as a basis for refusing to enforce arbitration clauses as written. Only this Court can supply an answer.

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[3] Respondents also stress that the class action waiver is non-mutual, but that is not literally true, as the class action waiver extends to all parties. Pet. App. 17a. The argument that the class waiver is effectively non-mutual is premised on the same policy argument that it is exculpatory -- that class action procedures benefit the consumer plaintiffs rather than defendants. *See Dunlap*, 567 S.E.2d at 278-80. Thus, any finding that the class action waiver was effectively non-mutual is premised on the same policy judgment that class procedures should be favored at the expense of arbitration agreements.

2. Respondents do not squarely address the second question presented for review -- whether questions of unconscionability should be decided by a court or arbitrator when the Arbitration Provision flatly states that questions of validity and enforceability of a provision should be decided by an arbitrator. Rather, respondents assert that this case is really about whether the trial court properly determined whether a contract existed at all. Opp. 1, 15, 18. This is baffling for two reasons. First, the trial court clearly held the Arbitration Provision was *unenforceable*, not that a contract never existed. Pet. App. 13a. Second, the question whether a court or arbitrator should decide if a contract containing an arbitration clause was validly formed was answered decades ago in *Prima Paint Corp.*, 388 U.S. at 404, which held that the question should go to the arbitrator. The question left open by *Prima Paint* and successive FAA cases is whether challenges to the substantive enforceability of an *arbitration clause* should be determined by a court or arbitrator. As we have shown, a series of recent cases suggests that issues regarding enforceability of an arbitration clause based on unconscionability or limitation of remedies should always go the arbitrator in the first instance. Pet. 19-21. On that question, the "circuit courts are split." *Investment Partners, L.P. v. Glamour Shots Licensing, Inc.*, 298 F.3d 314, 316 (5th Cir. 2002); *see* Pet. 21-23 (discussing circuit court decisions).[4] But the answer should be easy to discern where, as here, the parties expressly *agreed* that fights about the

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[4] Although respondents seem to suggest that these cases are inapplicable because they deal with the availability of remedies in arbitration, *see* Opp. 17, the dispute in this case over whether class action relief must be available to plaintiffs is clearly a question about a plaintiff's available remedies. This is apparent from the discussion of policy justifications for class relief in *Dunlap*, 567 S.E.2d at 272 n.3 & 278-79, and other state cases using similar reasoning to void arbitration clauses for lack of class-wide relief. *See* Pet. 13-14.

validity or enforceability of the arbitration clause should be arbitrated.

Contrary to respondents' discussion of these circuit court cases, *see* Opp. 17, the question whether a dispute over the unconscionability of an arbitration clause should go to a court or arbitrator is a question of federal law under the FAA, not at all dependent on state law principles. See Pet. 21-23. Whether or not West Virginia courts treat the question of contract formation as an equitable one to be decided by a court, the FAA may mandate a different approach -- either generally or at least where the parties so agreed. The trial court blithely ignored this issue. The Court should grant review to make clear that a court may not simply disregard the parties' agreement to allow an arbitrator to decide issues of enforceability, including unconscionability.

3. Respondents' remaining arguments also are not persuasive. Respondents contend that the court below provided adequate and independent grounds for affirming the judgment. Opp. 18-19. They rely both on the trial court's tortured interpretation of language in the arbitration provision regarding Block's contractual offset right to find the provision one-sided, discussed at Pet. 23-24, and two new arguments about whether there was a contract of adhesion and whether Block had standing to enforce the agreement. With respect to the latter two arguments, the court below simply did not rule on them and they are not presented for review. Moreover, all the arguments are encompassed by the second question presented in the Petition, which asks whether the trial court even had the authority to consider enforceability issues and interpret the contract language rather than defer to an arbitrator. If the court did not have this authority (and it should not, given the unambiguous language of the Arbitration Provision that disputes about the enforceability of the Provision should go to an arbitrator),

then the Court must vacate the trial court's interpretation of the contract language and remand to compel arbitration. *See Green Tree Financial Corp. v. Bazzle*, 539 U.S. 444 (2003); Pet. 24-25 & n.7.

Finally, respondents' jurisdictional argument is misguided. The Court has jurisdiction over a "final" judgment under 28 U.S.C. § 1257(a), and the trial court's decision satisfies the finality requirement by clearly resolving federal issues under the FAA that had been appealed to the highest state court possible. *See Southland Corp. v. Keating*, 465 U.S. 1, 6 (1984). Moreover, the fact that the case had been temporarily removed to federal court on the day the Petition was filed presents no jurisdictional obstacle whatsoever. Regardless of where the case was pending at the time of the Petition, the prior interlocutory order denying arbitration remained reviewable. Even if the case had remained in federal court -- and it did not -- petitioners would still have had the right to seek review on the arbitration issue. Respondents have not cited any authority remotely supporting their theory that the temporary removal undercut the finality and reviewability of the arbitration ruling.

CONCLUSION

The Petition for a writ of certiorari should be granted.

Respectfully submitted,

Matthew M. Neumeier
JENNER & BLOCK LLP
1 IBM Plaza
Chicago, IL 60611
(312) 222-9350

Paul M. Smith*
Duane C. Pozza
JENNER & BLOCK LLP
601 13th Street, N.W.
Washington, D.C. 20005
(202) 639-6000

*Counsel of Record

Counsel for Petitioners

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